No. 15245

In the United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA, APPELLANT

v.

HENRY W. MATTHEWS AND NETTIE MATTHEWS, DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF YUBA CITY LIVESTOCK AUCTION COMPANY, APPELLEES

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA, NORTHERN DIVISION

BRIEF FOR APPELLANT

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INDEX

CITATIONS

Cases:

412109—57——1

Cases—Continued

Cases—Continued

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JURISDICTIONAL STATEMENT

This action was brought by the United States against Henry W. and Nettie Matthews, doing business as Yuba City Livestock Auction Company to recover the reasonable market value ($1,526.22) of certain livestock which were subject to a valid chattel mortgage held by the Farmers Home Administration and which were sold by defendants without the knowledge or consent of the Administration (R. 3–7). The jurisdiction of the District Court over the action rested upon 28 U. S. C. 1345. On May 11, 1956, the United States District Court for the Northern Dis-

trict of California, Northern Division, entered judgment in favor of the United States in the amount of $46.79 (R. 32–33). On July 6, 1956, the Government filed notice of appeal (R. 33–34). The jurisdiction of this Court rests upon 28 U. S. C. 1291.

STATEMENT OF THE CASE

On March 17, 1951, one Wheaton executed a crop and chattel mortgage in favor of the Farmers Home Administration, an agency of the United States, on certain of his farm chattels, including the livestock which are the subject of this suit (R. 29). The mortgage, which represented security for a Production and Subsistence loan extended by the Farmers Home Administration[1] to Wheaton,[2] contained the customary provision that the mortgagor was not to sell any of the mortgaged property without first obtaining the consent of the mortgagee (R. 4, 28). It further provided that, upon the failure of the mortgagor to perform any of the covenants of the mortgage, the mortgagee was to become entitled to immediate possession of the mortgaged property (R. 11, 29). On the date of execution, the mortgage was duly recorded in Yuba County, California, the county in which

[1] Established under the Farmers Home Administration Act of 1946, 60 Stat. 1072, 7 U. S. C. 1001.

[2] The making of Production and Subsistence loans is authorized by Title II of the Bankhead-Jones Farm Tenant Act, 60 Stat. 1071, 7 U. S. C. 1007. Although not specifically described in the complaint, the loan extended to Wheaton was a Production and Subsistence loan. The forms executed by Wheaton, FHA 30—Crop and Chattel Mortgage and FHA 31—promissory note, are used by the Farmers Home Administration only for Production and Subsistence loans. 6 C. F. R., Chapter III, Subchapter C—"Production and Subsistence Loans," Sections 343.3 (e) and (i).

Wheaton then resided and in which the mortgaged property was then located (R. 11, 29).

Despite his obligation not to do so, between November 19, 1951, and March 2, 1953, Wheaton, without the consent or knowledge of appellant, periodically removed certain of the mortgaged livestock to adjoining Sutter County, California (R. 11, 29–30). The livestock were there delivered to appellees for sale by them at auction in the regular course of business (R. 11, 30). On each occasion, Wheaton warranted in writing that the animals delivered to appellees were free and clear of all liens and other encumbrances (R. 11, 30). Appellees did not have actual knowledge of the existence of the Farmers Home Administration mortgage (R. 11–12, 30).

Upon each sale, appellees turned the proceeds (which totalled $1,526.22) less their customary 3% commission (which totalled $46.79) over to Wheaton (R. 12, 30). Insofar as the record shows,[3] none of these proceeds were applied to Wheaton's debt to appellant, which debt is still due and owing in an amount in excess of $1,526.22 and cannot be satisfied out of Wheaton's current assets (R. 30–31).

On September 30, 1954, this action was brought in conversion against appellees to recover the reasonable market value of the sold livestock, *i. e.,* the price which had been received at auction (R. 3–7). On February 29, 1956, the District Court filed its memorandum opinion holding that appellant was entitled to recover from appellees only the commission which the latter had withheld (R. 10–27). Recognizing that, under

[3] See, however, p. 32, *infra*, fn. 17.

California law, appellees would be liable to appellant for the full market value of the livestock, the court determined that federal law governed (R. 21–25). Relying on the decision of the United States District Court for the Northern District of Iowa in *Drover's Cattle Loan & Investment Co.* v. *Rice,* 10 F. 2d 510, the court then ruled that under federal law a commission merchant is liable to the mortgagee in these circumstances solely for that portion of the proceeds of the sale which are retained by him (R. 25–27).

On May 11, 1956, judgment was entered in favor of appellant in the amount of $46.79 (R. 32–33). This appeal followed (R. 33–34).

QUESTIONS PRESENTED

1. Whether appellees' liability in conversion to appellant is governed by federal or state law.

2. Whether, in the circumstances of this case, federal law imposes liability in conversion upon appellees for the reasonable value of the mortgaged livestock which appellees sold without the knowledge or consent of the appellant mortgagee.

SPECIFICATION OF ERRORS RELIED ON

1. The District Court erred in holding that, under federal law, appellees were not liable in conversion to appellant for the reasonable market value of the livestock mortgaged to Farmers Home Administration, which they sold without the consent or knowledge of the mortgagee.

2. The District Court erred in holding that the liability of appellees was limited to the amount of the commission they received for the sale of the mortgaged livestock.

3. The District Court erred in not entering judgment for appellant in the amount of $1,526.22, the reasonable market value of the mortgaged livestock which they sold without the consent or knowledge of the mortgagee, less any amount that the mortgagor may have subsequently refunded to appellant out of the proceeds of the sales.

ARGUMENT

Appellees are liable in conversion for the full value of the mortgaged livestock here involved, less any amount refunded to appellant out of the proceeds of the sales

Introduction and summary

This case presents the identical issues which were recently before the Court of Appeals for the Eighth Circuit in *United States* v. *Kramel,* 234 F. 2d 577. In that case, the District Court had determined that, by reason of *Erie* v. *Tompkins,* 304 U. S. 64, the question as to whether a commission merchant is liable in conversion in the present circumstances is governed by state law. It then applied, with expressed reluctance, a decision of an intermediate appellate court of the State of Missouri (the state in which the alleged conversion took place) which construed the Federal Packers and Stockyards Act, 7 U. S. C. 201, *et seq.,* as

barring any action in conversion against a livestock commission merchant or "market agency."[4]

The Court of Appeals affirmed. While agreeing with the Government that *Erie* v. *Tompkins* is applicable solely to cases where jurisdiction is grounded upon diversity of citizenship,[5] the court held that state law nevertheless was controlling (234 F. 2d at 580–583). In its view, nothing in the Farmers Home Administration Act of 1946, which established the Administration, reflects a Congressional intent that a uniform federal rule is to be applied in determining the extent of the Government's right to enforce security given to it in connection with loans made by the Administration (234 F. 2d at 580–581).

If the *Kramel* holding that state law controls is correct, it perforce follows that appellant is entitled to recover here the value of the mortgaged livestock

[4] The District Court concluded: "Therefore, under compulsion of [*Blackwell* v. *Laird*, 236 Mo. App. 1217, 163 S. W. 2d 91], and against the great weight of authority, and against my own judgment of what law on the point ought to be [the commission merchants' motion to dismiss the complaint] must be, and it is hereby sustained."

Blackwell v. *Laird* holds that since the Packers and Stockyards Act "prohibits discrimination" against any consignor by a market agency, the court will not penalize a commission merchant for selling stolen or mortgaged property by holding it liable in conversion.

[5] The correctness of this view of the limited scope of Erie requires no extended discussion. See *Guaranty Trust Co.* v. *York*, 326 U. S. 99, 1109; *Cohen* v. *Beneficial Loan Corp.*, 337 U. S. 541, 555; *United States* v. *Standard Oil Co.*, 332 U. S. 301, 307; *D'Oench, Duhme & Co.* v. *FDIC*, 315 U. S. 447, 467 (concurring opinion of Mr. Justice Jackson); *American Textile Machine Co.* v. *United States*, 220 F. 2d 584, 587 (C. A. 6); *Siegelman* v. *Cunard White Star*, 271 F. 2d 189, 192 (C. A. 2).

which appellees sold without the consent or knowledge of the Farmers Home Administration—less, of course, any portion of the proceeds which the mortgagor may have refunded to appellant out of the proceeds of the sales (see p. 32, *infra,* fn. 17). As the court below conceded (R. 21), under California law a commission merchant is liable in conversion to the holder of a duly recorded chattel mortgage, whether or not he possesses actual knowledge of the lien at the time the mortgaged property is sold. *Swim* v. *Wilson,* 90 Cal. 126; *Lusitanian-American Development Co.* v. *Seaboard Dairy Credit Corp.,* 1 Cal. 2d 121, 34 P. 2d 139.

Despite this consideration, we do not urge this Court to adopt *Kramel.* To the contrary, it is our position, developed in Point I below, that the Eighth Circuit decision on the matter of choice of law is wrong and the District Court here correctly ruled that federal law is to be looked to.

We show in Point II, however, that the court below erroneously determined that, under federal law, appellees are not liable in conversion to appellant. The federal common law in this area is that common law rule which is generally recognized in the United States. And this general rule is reflected by the California holdings—namely, commission merchants and livestock auctioneers as well as other individuals who sell property which is covered by a duly recorded, valid mortgage are liable in conversion to the mortgagee. The Missouri view otherwise notwithstanding, there is nothing in the Federal Packers and Stockyards Act which calls for a departure from the settled rule. Further, the few decisions which exonerate the

commission merchant on other grounds are equally unsound.

We also show in Point II that there is an additional reason why the general rule should be accepted as constituting federal law. By virtue of 18 U. S. C. 658, it is a felony intentionally to convert property mortgaged to the Farmers Home Administration. While it may be that there was no criminal conversion here on the part of appellees, Section 658 manifests a clear Congressional policy of protecting the Farmers Home Administration from both intentional and non-intentional conversion of its collateral and from the resulting loss of public moneys. This policy should have been, but was not, taken into consideration by the court below in fashioning the federal rule.

I

The District Court correctly held that appellees' liability is governed by federal law

A. The loan secured by the mortgage in issue here was made under a vast nationwide lending program

The Production and Subsistence Loan underlying the chattel mortgage here involved was an integral part of the Production and Subsistence Loan Program carried out by the Farmers Home Administration[6] under the authority of Title II of the Bankhead-Jones Farm Tenant Act, 7 U. S. C. 1007, *et seq.* The objective of this loan program is to enable farmers and stockmen "to become established successfully in a

[6] The Farmers Home Administration was established by the Farmers Home Administration Act of 1946, 60 Stat. 1072, 7 U. S. C. 1001.

sound, well balanced system of farming in order to make full and efficient use of their land and labor resources" (6 C. F. R. 342.1 (a)). Toward this end, eligible farmers may obtain loans from the Farmers Home Administration for soil conservation and improvement measures, the purchase of livestock, farm equipment, repairs, feed and insecticides, payment of farm help, cash rent, debts secured by liens, farm buildings, and the meeting of family subsistence needs (6 C. F. R. 342.3).

On applying for a Production and Subsistence Loan, the borrowing farmer must certify in writing that he cannot obtain sufficient credit to meet his needs at rates (not exceeding 5% per annum) and terms for loans of similar size and character in or near the community in which he lives (6 C. F. R. 342.2 (b)). Once a loan application is approved, the borrower must execute a promissory note, standard form FHA–31,[7] which he is required to repay within seven years of the date of the loan (6 C. F. R. 342.4 (b)). At the time the funds are turned over to the borrower, he must also execute a standard form FHA–30 "crop and chattel mortgage,"[8] which provides for a lien in favor of the United States on as much of the livestock and farm equipment of security value owned by the borrower at the time the loan is made as is necessary to protect the interests of the Government (6 C. F. R. 342.5 (c)). The chattel mortgage, a United States Government Printing Office form which contains the same general terms no matter where it is executed,

[7] 6 C. F. R. 343.3 (f).
[8] 6 C. F. R. 343.3 (j).

is then filed or recorded in the county in which the borrower's farm is located (6 C. F. R. 343.5 (c)).

The extensiveness of the loan program is amply reflected by available statistical data. Between March 1, 1946, and June 30, 1953, a total of $614,021,110 was loaned to farmers in every state of the Union, Alaska, Hawaii, Puerto Rico, and the Virgin Islands. Of this amount, almost $11,000,000 represented loans in the State of California alone.[9]

B. In the absence of an express statutory provision to the contrary, Federal law governs the rights and liabilities of the United States in the administration of programs of this character

1. The Supreme Court has consistently recognized that where the United States, acting pursuant to the Constitution, Acts of Congress, or treaties, enters into large scale transactions requiring uniform administration, questions of federal rights and liabilities must be uniformly determined by reference to federal law.[10] *Board of Commissioners* v. *United States,* 308 U. S. 343; *Clearfield Trust Co.* v. *United States,* 318 U. S. 363; *United States* v. *Allegheny County,* 322 U. S. 174; *United States* v. *Standard Oil,* 332 U. S. 301. Cf. *Bank of America* v. *Parnell,* 352 U. S. 29. Indeed the

[9] Report of the Loan, Collection and Debt Adjustment Activities, United States Department of Agriculture, Farmers Home Administration, 1954; Report of the Administrator of the Farmers Home Administration, U. S. Department of Agriculture, 1953, p. 24.

[10] Where a federal policy or federal statutes are involved in lawsuits between private litigants, the courts have likewise recognized that federal law must control. *Sola Electric Co.* v. *Jefferson Electric Co.*, 317 U. S. 173; *Holmberg* v. *Armbrecht*, 327 U. S. 392; *Dice* v. *Akron C. & Y. R. Co.*, 342 U. S. 359; *Prudence Corp.* v. *Geist*, 316 U. S. 89; Moore's *Commentary on the U. S. Judicial Code*, pp. 309, 340.

very purpose of the supremacy clause in the Rules of Decision Act, 28 U. S. C. 1652,[11] "was to avoid the introduction of disparities, confusions and conflicts which would follow if the Government's general authority were subject to local controls" through the application of state law. *United States* v. *Allegheny County,* 322 U. S. 174, 183. Thus in *Clearfield Trust Co.* v. *United States,* 318 U. S. 363, state law was held inapplicable in an action by the United States on a check issued by the United States Treasury. The Supreme Court held that since the United States exercises a constitutional function or power in issuing commercial paper, and since the issuance of commercial paper by the United States is on a vast scale, federal law must be applied to determine the rights and liabilities of the Government in this regard. Said the Court [318 U. S. at 366–367]:

> We agree with the Circuit Court of Appeals that the rule of *Erie R. Co.* v. *Tompkins,* 304 U. S. 64, does not apply to this action. The rights and duties of the United States on commercial paper which it issues are governed by federal rather than local law. When the United States disburses its funds or pays its debts, it is exercising a constitutional function or power. This check was issued for services performed under the Federal Emergency Relief Act of 1935, 49 Stat. 115. The authority to issue the check had its origin in the Constitution and the

[11] The Rules of Decision Act, 28 U. S. C. 1652, provides: "The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply."

statutes of the United States and was in no way dependent on the laws of Pennsylvania or any other state. Cf. *Board of Commissioners* v. *United States,* 308 U. S. 343; *Royal Indemnity Co.* v. *United States,* 313 U. S. 289. The duties imposed upon the United States and the rights acquired by it as a result of the issuance find their roots in the same federal sources. Cf. *Deitrick* v. *Greaney,* 309 U. S. 190; *D'Oench, Duhme & Co.* v. *Federal Deposit Ins. Corp.,* 315 U. S. 447. In absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards. * * *

In our choice of the applicable federal rule we have occasionally selected state law. See *Royal Indemnity Co.* v. *United States, supra.* But reasons which may make state law at times the appropriate federal rule are singularly inappropriate here. The issuance of commercial paper by the United States is on a vast scale and transactions in that paper from issuance to payment will commonly occur in several states. The application of state law, even without the conflict of laws rules of the forum, would subject the rights and duties of the United States to exceptional uncertainty. It would lead to great diversity in results by making identical transactions subject to the vagaries of the laws of the several states. The desirability of a uniform rule is plain. And while the federal law merchant, developed for about a century under the regime of *Swift* v. *Tyson,* 16 Pet. 1, represented general commercial law rather than a choice of a federal rule designed to protect a federal right,

it nevertheless stands as a convenient source of reference for fashioning federal rules applicable to these federal questions.

United States v. *Allegheny County,* 322 U. S. 174, represents an extension of the *Clearfield* case to cover all cases involving contracts entered into by the United States. The question in *Allegheny* was whether, for the purposes of state taxation, Pennsylvania law determined title to machinery leased by the United States to a war contractor. The Supreme Court rules that state law was inapplicable, holding that the terms of the contract must be construed according to federal law. "The validity and construction of contracts through which the United States is exercising its constitutional functions, their consequences on the rights and obligations of the parties, the titles or liens which they create or permit, all present questions of federal law not controlled by the law of any state," (*id.* at 183). And in *United States* v. *Standard Oil Co.,* 332 U. S. 301, the rule of *Clearfield* and its companion cases was held applicable where, as here, "the relations affected are noncontractual or tortious in character" (*id.* at 305).

2. In ruling in *United States* v. *Kramel,* 234 F. 2d 577, that state law was controlling, the Eighth Circuit gave virtually no consideration to the above cases. Instead, although conceding that there was merit in the Government's position that the Production and Subsistence Lending Program requires uniform administration, the court restricted itself to an examination of the terms of the Farmers Home Administration Act (234 F. 2d at 580–581). Finding no express

provision therein to the effect that federal law is to govern, the court drew the inference that Congress intended state law to be controlling.

This inference, we submit, will not stand analysis. To the contrary, if any conclusion may be properly drawn from the silence of Congress with respect to choice of law, it is that Congress intended that federal law was to be resorted to. This follows from the fact that where Congress has desired state law to control on some facet of the administration of a federal statute of widespread applicability, the statute itself has generally so provided. For example, the Social Security Act stipulates that an applicant's status as the wife of the deceased employee is to be determined by reference to state law (Act of August 28, 1950, c. 809, Title I, Section 104 (a), 64 Stat. 511, 42 U. S. C. 416 (h) (1)). Similarly, governmental liability under the Federal Tort Claims Act is, subject to certain exceptions, determined by the extent, if any, to which "the United States, if a private person, would be liable to the claimant in accordance with the law of the place where the [misconduct] occurred" (28 U. S. C. 1346 (b)). See also, Section 209 (b) of the Federal Coal Mine Safety Act, 30 U. S. C. 479 (b) (state law governs on question as to whether a mine is "gassy" or "gaseous"); Section 7 (c) of the National Banking Act, 12 U. S. C. 36 (c) (establishment of branches by national banks subject to authorization by state statute and to location restrictions imposed by state law on state banks).

In this connection it is to be noted that in the heretofore discussed Supreme Court cases, holding state

law inapplicable, the court did not deem—and could not have consistent with the result it reached—the critical inquiry to be whether there was a specific expression of legislative intent that federal law was to control. Rather, as we have seen, the determinative considerations were (1) that the governmental activity involved was one of vast breadth and scope; and (2) that, since, as a consequence, reference to state law would make "identical transactions subject to the vagaries of the laws of the several states * * *, [t]he desirability of a uniform rule is plain." *Clearfield Trust Co.* v. *United States,* 318 U. S. at 367. As the Supreme Court observed in *United States* v. *Standard Oil* (where the Government sought to recover the expense it incurred when a member of the military service was injured through the defendant's negligence) [332 U. S. at 310–311]:

> * * * [T]he principal, if not the only, effect of [the liability sought] would be to make whole the federal treasury for financial losses sustained, flowing from the injuries inflicted and the Government's obligations to the soldier. The question, therefore, is chiefly one of federal fiscal policy, not of special or peculiar concern to the states or their citizens. And because those matters ordinarily are appropriate for uniform national treatment rather than diversified local disposition, as well where Congress has not acted affirmatively as where it has, they are more fittingly determinable by independent federal judicial decision than by reference to varying state policies.

We stress again that these considerations are equally present in this case.

Further, the Eighth Circuit's expressed reluctance in *Kramel* with respect to "replacing State tort laws affecting property rights" (234 F. 2d at 581) is equally irreconcilable with the relevant Supreme Court holdings. The effect of the Supreme Court's decision in *Clearfield,* for example, was to displace, insofar as Government commercial paper is concerned, state negotiable instrument laws no less affecting property rights. And if the Eighth Circuit's intended emphasis was on the fact that conversion is an action in tort, rather than in contract, *United States* v. *Standard Oil Co.,* of course, provides the total answer.

II

Appellees are liable in conversion under federal law

For the foregoing reasons, we agree with the court below that California law, as such, is not applicable here. At the same time, we submit that the court plainly erred in holding that, under federal law, appellees' sale of livestock subject to a duly recorded, valid chattel mortgage held by the Farmers Home Administration did not give rise to liability in conversion to the United States.

A. The generally accepted common law rule imposes liability on livestock commission merchants in these circumstances

In *Clearfield Trust Co.* v. *United States, supra,* the Supreme Court pointed out that, while in cases of this character it is for the federal courts to fashion the governing rule of law according to their own standards, general commercial law principles are an

appropriate source of reference. And in *United States* v. *Butt,* 203 F. 2d 643, which like this case was a suit by the United States for the conversion of property on which it held a duly recorded chattel mortgage, the Tenth Circuit determined the right of the Government to recovery by looking to the generally recognized common law rule. This rule, the court found in resolving the conversion issue in favor of the United States, is that (203 F. 2d at 644–645) "[A] mortgagee who has suffered a loss may maintain an action against a person who has wrongfully converted to his own use property included in the mortgage which has been duly filed for record."

That the *Butt* case represents a correct application of general principles of the law merchant is clear. In virtually all states, including California where appellees conduct their business (see p. 7, *supra*), "[a] purchaser of property upon which there is a valid [recorded or filed] chattel mortgage who consumes or sells the property or any part of it is liable to the mortgagee for the damages so occasioned him" (2 *Jones on Chattel Mortgages* (1933) Section 490).[12]

[12] *Walters* v. *Slimmer*, 272 Fed. 435 (C. A. 7), under the Illinois law; *Denver Live Stock Comm. Co.* v. *Lee*, 18 F. 2d 11, 20 F. 2d 531 (C. A. 8), apply the Colorado law; *Sternberg* v. *Strong*, 158 Ark. 419, 250 S. W. 344; *Adamson* v. *Moyes*, 32 Idaho 469, 184 Pac. 849; *Twin Falls Bank &c. Co.* v. *Weinberg*, 44 Idaho 332, 257 Pac. 31, 54 A. L. R. 1527; *Lawton* v. *Ewing*, 240 Ill. App. 607. *Duke* v. *Strickland*, 43 Ind. 494; *McFadden* v. *Hopkins*, 81 Ind. 459; *Ross* v. *Menefee*, 125 Ind. 432, 25 N. E. 545; *United States Nat. Bank* v. *Great Western Sugar Co.*, 60 Mont. 342, 199 Pac. 245; *Beers* v. *Waterbury*, 21 N. Y. Super. Ct. 396; *More* v. *Western Grain Co.*, 37 N. Dak. 547, 164 N. W. 294; *Bank of Norris* v. *Pates &c. Co.*, 108 S. C. 361, 94 S. E. 881; *Little* v. *Southern Cotton Oil Co.*, 156 S. C. 480, 153 S. E. 462; *Bank of Brookings* v. *Aurora*

"An absolute sale of the mortgaged property by the mortgagor or anyone claiming under him, in exclusion of the rights of the mortgagee, is a conversion of it for which the mortgagee may maintain trover.[13] * * * If a mortgagor, for the purpose of defrauding the mortgagee, sends the mortgaged goods to an auctioneer, by whom they are sold, and the proceeds paid over to the mortgagor, the mortgagee may maintain trover *against the auctioneer,* although the latter did not participate in the fraud and had no knowledge of the existence of the mortgage * * *. *A commission*

Grain Co., 45 S. D. 113, 186 N. W. 563; *First Nat. Bank of Pipestone* v. *Siman*, 65 S. D. 514, 275 N. W. 347; *Western Mfg. &c.* v. *Shelton*, 8 Tex. Civ. App. 550, 29 S. W. 494, construing Texas statute: *Moore-Hustead Co.* v. *Moon Buggy Co.* (Tex. Civ. App.), 221 S. W. 1032; *First Nat. Bank* v. *Davis* (Tex. Civ. App.), 5 S. W. 2d 753. Where the mortgaged property was sold by the mortgagor without the consent of the mortgagee, and resold by the purchaser, the successive buyers are jointly liable for a conversion. *Union State Bank* v. *Warner*, 140 Wash. 220, 248 Pac. 394.

[13] *Heflin* v. *Slay*, 78 Ala. 180; *Sternberg* v. *Strong*, 158 Ark. 419, 250 S. W. 344 (both mortgagor and purchaser are liable for the sale and purchase of a part of the mortgaged property, made without the consent of the mortgagee); *Mitchell* v. *Mason*, 184 Ark. 1000, 44 S. W. 2d 672; *Ashmead* v. *Kellogg*, 23 Conn. 70; *Brown* v. *Campbell*, 44 Kans. 237, 24 Pac. 492; *Whitney* v. *Lowell*, 33 Maine 318; *American Agro Chemical Co.* v. *Small*, 129 Maine 303, 151 Atl. 555; *Coles* v. *Clark*, 3 Cush (57 Mass.) 399; *Chamberlin* v. *Clemence*, 8 Gray (74 Mass.) 389; *Lafayette County Bank* v. *Mitcalf*, 40 Mo. App. 494; *White* v. *Phelps*, 12 N. H. 382; *Wilson* v. *Russell*, 144 Okla. 284, 290 Pac. 1106; *Hill* v. *Winnsboro Granite Corp.*, 112 S. C. 243, 99 S. E. 836; *Cone* v. *Ivinson*, 4 Wyo. 203, 33 Pac. 31, 35 Pac. 933; *Security State Bank* v. *Clovis Mill & Elev. Co.*, 41 N. Mex. 341, 68 P. 2d 918; *Allis Chalmers Mfg. Co.* v. *Security Elev. Co.*, 140 Kans. 580, 38 P. 2d 138; *First Nat. Bank of Pipestone* v. *Siman*, 65 S. D. 514, 275 N. W. 347 (commission merchants held liable to mortgage in conversion for sale of mortgaged sheep, even though they had no notice of the mortgage).

merchant is under the same liability in this respect as an auctioneer. Although he sells mortgaged property without any notice of a duly recorded mortgage, he is liable in tort for conversion to the mortgagee".[14] (2 *Jones on Chattel Mortgages* (1933), Section 460). [Emphasis supplied.]

B. The Packers and Stockyards Act does not give rise to an exception to the general rule

Contrary to the holding of the Missouri intermediate appellate court in *Blackwell* v. *Laird,* 236 Mo. App. 1217, 163 S. W. 2d 91, the requirement in Section 205 of the Federal Packers and Stockyards Act, 7 U. S. C. 205 that: "It shall be the duty of every stockyard owner and market agency to furnish upon reasonable request, without discrimination, reasonable stockyard services * * *" does not have any effect upon this settled rule. As the Supreme Court itself observed in *Stafford* v. *Wallace,* 258 U. S. 495, 514–515, the purpose of the Act is to secure:

> The free and unburdened flow of livestock from the ranges and farms of the West and

[14] *Sig Ellingson & Co.* v. *DeVries*, 199 F. 2d 677 (C. A. 8) (applying the law of Minnesota); *Sig Ellingson & Co.* v. *Butenbach*, 199 F. 2d 679 (C. A. 8); *Wisdom* v. *Keithley*, 167 S. W. 2d 450 (St. Louis Court of Appeals, 1943); *Birmingham* v. *Rice Bros.*, 238 Iowa 410, 26 N. W. 2d 39; *Citizens State Bank* v. *Farmers Union Livestock Coop. Co.*, 165 Kans. 96, 193 P. 2d 636; *Mason City Production Credit Assn.* v. *Sig Ellingson & Co.*, 205 Minn. 537, 286 N. W. 713, certiorari denied, 308 U. S. 599, motion for rehearing of the petition denied, 308 U. S. 637; *Moderie* v. *Schmidt*, 6 Wash. 2d 592, 108 P. 2d 331; *First Nat. Bank of Pipestone* v. *Siman*, 67 S. Dak. 118, 289 N. W. 416; *Walker et al.* v. *Caviness et al.*, 256 S. W. 2d 880 (Tex. Civ. App.). *Seymour et al* v. *Austin et al.*, 101 F. Supp. 915 (D. Ore.); *Driver* v. *Mills*, 86 A. 2d 724 (Md.); 2 A. L. R. 2d 1124.

> the Southwest through the great stockyards and slaughtering centers on the borders of that region, and thence in the form of meat products to the consuming cities of the country * * * or, still as livestock, to the feeding places and fattening farms * * *. The chief evil feared is the monopoly of the packers, enabling them unduly and arbitrarily to lower prices to the shipper who sells, and unduly and arbitrarily to increase the price to the consumer who buys. Congress thought that the power to maintain this monopoly was aided by control of the stockyards. Another evil which it sought to provide against by the act, was exorbitant charges, duplication of commissions, deceptive practices in respect to prices, in the passage of the livestock through the stockyards, all made possible by collusion between the stockyards management and the commission men, on the one hand, and the packers and dealers on the other.

From this reading of the legislative purpose, there is virtually universal agreement that:

> Congress did not adopt the Packers and Stockyards Act to encourage and protect the operation of fences for handling property stolen or procured by fraud. The Act merely makes it the duty of [commission merchants] to furnish upon *reasonable request without discrimination* reasonable stockyards services. It is not wrongful discrimination to refuse to aid a criminal in his crime, nor is a request that one dispose of property fraudulently procured or stolen a *reasonable request.*

Birmingham v. *Rice Bros.,* 238 Iowa 410, 417–418, 26 N. W. 2d 39, 43. [Emphasis in original.] Accord:

Mason City Production Credit Assn. v. *Sig Ellingson & Co.,* 205 Minn. 537, 286 N. W. 713, certiorari denied, 308 U. S. 599, motion for rehearing of petition denied, 308 U. S. 637; *Sig Ellingson & Co.* v. *DeVries,* 199 F. 2d 677 (C. A. 8); *Sig Ellingson & Co.* v. *Butenbach,* 199 F. 2d 679 (C. A. 8); *First Nat. Bank of Pipestone* v. *Siman,* 67 S. Dak. 118, 289 N. W. 416; *Citizens State Bank* v. *Farmers Union Livestock Coop. Co.,* 165 Kans. 96, 193 P. 2d 636; *Moderie* v. *Schmidt,* 6 Wash. 2d 592, 108 P. 2d 331; *Walker, et al.* v. *Caviness, et al.,* 256 S. W. 2d 880 (Tex. Civ. App.); *Seymour, et al.* v. *Austin, et al.,* 101 F. Supp. 915 (D. Ore.); *Driver* v. *Mills,* 86 A. 2d 724, 727 (Md.). In the *Moderie* case, the Supreme Court of Washington commented thusly upon the denial of certiorari in *Mason City:* "We note that the Solicitor General of the United States appeared in the Supreme Court and opposed granting of the writ. It seems reasonable to infer that the decision of the Minnesota Supreme Court was satisfactory to the federal authorities charged with the administration of the Packers and Stockyards Act." 108 P. 2d at 334.

No state court construction of a federal statute is, of course, binding on this or any other federal tribunal. *Board of Commissioners* v. *United States,* 308 U. S. 343; *Lyeth* v. *Hoey,* 305 U. S. 188; *Prudence Corp.* v. *Geist,* 316 U. S. 89; *Awotin* v. *Atlas Exchange Bank,* 295 U. S. 209; *Austrian* v. *Williams,* 216 F. 2d 278, 281 (C. A. 2); Rules of Decision Act, 28 U. S. C. 1652; Moore's *Commentary on the U. S. Judicial Code,* p. 309. We submit, however, that these latter

cases—and not *Blackwell*—reflect the correct view of the function of the Packers and Stockyards Act in general and Section 205 in particular. And in this regard, it is worthy of mention in passing that there is even doubt as to whether the Eighth Circuit in *Kramel* properly regarded *Blackwell* as representing Missouri law on the subject. Less than a year after the Kansas City Court of Appeals decided that case, the St. Louis Court of Appeals held a commission merchant liable in conversion in these precise circumstances. *Wisdom* v. *Keithley,* 167 S. W. 2d 450. While not alluding in its opinion either to *Blackwell* or to the Packers and Stockyards Act, the court observed that [167 S. W. 2d at 457]:

> [The commission merchants] were found to have acted innocently and without actual knowledge of the existence of the mortgage, but they are nonetheless personally liable to [the mortgagee] for the conversion of the steers. It was their business, as [the mortgagor's] agents, to ascertain his right to have the steers sold at the auction they conducted, and it is no defense for them to say that they acted under [the mortgagor's] authority, when the fact was that [the mortgagor] had no authority. However innocent they were of [the mortgagee's] claim, and however unaware they were of [the mortgagor's] lack of right to sell, [the commission merchants], by selling the mortgaged steers and remitting the proceeds to [the mortgagor], they became participants in the conversion, and are equally liable with the other defendants who were the purchasers of the steers.

This, as we have seen, is nothing more than a statement of the majority rule.[15]

C. The general rule is supported by reason as well as the overwhelming weight of authority

1. As justification for its refusal to follow the general rule respecting the liability of commission merchants, the court below pointed (R. 25) to the decision of the District Court for the Northern District of Iowa in *Drover's Cattle Loan and Investment Co.* v. *Rice,* 10 F. 2d 510. In that case, the court followed the early Tennessee holding in *Frizzell* v. *Rundle,* 88 Tenn. 396, 12 S. W. 918, to the effect that, since the commission merchant is acting merely in the capacity of an agent, he may not be held responsible to the mortgagee in the absence of actual knowledge of the existence of the lien.

To our knowledge, apart from the *Drover's* case, *Frizzell* v. *Rundle* has been adopted on the issue of the liability of a livestock commission merchant only by a Mississippi court—and there by way of dictum. *Dixie Stock Yard* v. *Ferguson,* 192 Miss. 166, 4 So. 2d 724. In virtually every other jurisdiction that has had occasion to consider this issue, *Frizzell* has

[15] The Missouri Supreme Court has not passed directly upon this question. In September 1955, however, that court cited with approval the portion of the district court opinion in *DeVries* v. *Sig Ellingson & Co.*, 100 F. Supp. 781 (D. Minn.), affirmed, 199 F. 2d 677 (C. A. 8) to the effect that the Packers & Stockyards Act was not designed to supersede well established principles of chattel mortgage law. *Houfberg* v. *Kansas City Stockyards Co. of Maine*, 283 S. W. 2d 539, 543–544. In view of this fact, it is subject to considerable question that, should the conflict between *Wisdom* and *Blackwell* reach it at some point, the latter will be adopted by the Missouri Supreme Court.

been expressly or implicitly rejected. For example, in *First National Bank of Pipestone* v. *Siman,* 65 S. Dak. 514, 275 N. W. 347, 349, *Frizzell* was characterized as not only opposed to the great weight of authority but, in addition, unsound in principle. On the latter score, the South Dakota court referred to the basic rule of agency law that "an agent who does acts which would otherwise constitute conversion of a chattel is not relieved from liability by the fact that he acts on account of his principal and reasonably, although mistakenly, believes that the principal is entitled to possession of the chattel." *Restatement of the Law of Agency,* Section 349. See, also, *Meacham on Agency* (2d Ed., 1914), Section 1457.

Drover's in no way representing general commercial law (cf. *Clearfield, supra,* pp. 12–13), and in the absence of compelling reasons for repudiating the view of the overwhelming majority of courts, the court below should not have taken it as reflecting the appropriate rule for uniform application throughout the United States in circumstances where federal law governs. We now show that no such compelling reasons exist; that, instead, there is a good and substantial basis, quite apart from the matter of precedential support, for holding appellees liable in conversion as a matter of federal law.

2. The court below suggested (R. 19–20) that, underlying the result in *Frizzell* and *Drover's,* was a belief that it is burdensome for a commission merchant to ascertain the status of the title to livestock brought to him for sale; and that, if he is required to assume that burden to avoid possible liability in

conversion, the necessary effect will be an increase in the commission which is charged for his services. If, however, these were in fact the considerations deemed dispositive by the court in those cases, we submit that they are far outweighed by the deleterious consequences flowing from the immunization of the commission merchant from liability.

As significant as may be the commission merchant's function in our economy, it is assuredly of no greater importance than the economic function which is performed by those who, in the first instance, finance the raising and feeding of the livestock which are marketed through the commission merchant. And, as the Supreme Court of a leading meat packing state pointed out in the course of holding a commission merchant liable to the mortgagee, it is "common knowledge" not only that meat producers (such as Wheaton here) often must obtain loans to carry on their business but, additionally, that this credit can be obtained only "by giving as security chattel mortgages upon the stock being raised and fed for the market." *Mason City Production Credit Ass'n.* v. *Sig Ellingson and Co.,* 205 Minn. 537, 542, 286 N. W. 713, 716, certiorari denied, 308 U. S. 599, motion for rehearing denied, 308 U. S. 637. The accuracy of this observation is underscored by the fact that Congress found it necessary in the public interest to establish a vast lending program to aid the marginal producer unable to obtain credit through private sources at locally prevailing rates of interest, the security for the specific loan being all that the producer customarily has to offer—namely a lien on his livestock, crops and

whatever farm equipment he may possess that is not already mortgaged to the extent of its value. See pp. 8–10, *supra*.

It goes without saying that, absent an effective means for its enforcement, the lien which the lendor obtains as an essential part of the *quid pro quo* for the loan is of little value. And where the security is primarily or exclusively livestock, and the borrower converts it, it is equally plain that the only effective means available for collection of the underlying debt is to look to those—including, if not principally, the commission merchant—who have had some part in the conversion. For the livestock itself will, by the very nature of things, be slaughtered and processed upon its sale, often long before the lendor becomes aware of the borrower's violation of the mortgage agreement.

We think that the fact that the overwhelming majority of both meat producing and meat packing states permit the mortgagee to proceed against the commission merchant in conversion reflects a recognition that an opposite result would transform what were intended to be secured loans into an unsecured lending operation and thus severely restrict the future availability of credit to livestock producers. Implicit, too, in the wide acceptance of the general rule is the realization that, unlike the creditor, the commission merchant is in a position to protect himself—either through an appropriate inquiry into the vendor's title, or, if such is not feasible in the particular situation, through insurance against the contingency of a defect in that title. Presumably, most commission merchants in states such as California, Iowa,

Kansas and Minnesota have undertaken satisfactory protective measures against liability in conversion and have found them to involve no undue burden or expense. This is at least a permissible inference from the fact that there has not been a successful effort (if in fact some serious effort has been made) in any of those jurisdictions to overturn the majority rule, either by legislative enactment or otherwise. Certainly, if that rule proved to be inequitable or unworkable, it would not long have been enforced.

D. Acceptance of the general rule is further called for by the announced congressional policy in this area

Leaving aside the above considerations, we think that there is another and independent reason why the court below erred in not holding appellees liable to the United States, as a matter of federal law, for the full value of the mortgaged livestock which they sold without the Farmers Home Administration's consent. As we have noted, in aiding farmers the Government lends money on terms and conditions that are not acceptable to local lending agencies, taking collateral of a less durable type such as livestock and crops. Because of the scope of the program, the Administration does not enjoy even such opportunity as a local private lending institution may have to investigate, check, and foreclose as soon as a borrowing farmer converts mortgaged property. To protect the Farmers Home Administration from conversion and unauthorized disposition of its collateral and from the resultant loss of public funds, Congress has enacted a statute which imposes criminal sanctions on any person who knowingly converts property

mortgaged to the United States. In pertinent part, 18 U. S. C. 658 provides: "Whoever, with intent to defraud, knowingly conceals, removes, disposes of, or converts, to his own use or to that of another, any property mortgaged or pledged to or held by * * * The Secretary of Agriculture acting through the Farmers Home Administration * * * shall be fined not more than $5,000 or imprisoned not more than five years, or both * * *." Clearly, if appellees, *knowing* that the livestock consigned to them by Wheaton was mortgaged to the United States, took the livestock for sale and turned the proceeds over (as they did) to Wheaton, they would be guilty of a felony under 18 U. S. C. 658. Here, we are dealing not with a criminal violation of that statute, but with an act implicitly condemned by it. Certainly, a congressional intent to protect the Farmers Home Administration from criminal conversions is clear on the face of the Act. No less clear, we maintain, is a congressional policy of protecting the Administration from nonintentional or noncriminal conversions of its collateral and from the resulting loss of public money. Questions as to the extent and nature of the legal consequences of this statutory condemnation not only are questions of federal and not state law but, additionally, must be resolved in the light of the federal policy clearly announced in Section 658. *Deitrick* v. *Greany,* 309 U. S. 190, 200–201; *D'Oench, Duhme & Co.* v. *F. D. I. C.,* 315 U. S. 447.

In the *Deitrick* case, *supra,* the Supreme Court held that the maker of an accommodation note executed to conceal a stock purchase transaction for-

bidden by the National Banking Act was estopped on the ground of public policy, as announced in that Act, to deny lack of consideration in a suit by a receiver of the payee national bank. Specifically rejecting the argument that it was necessary to prove an equitable estoppel the court held that "It is the evil tendency of the prohibited acts at which the statute is aimed, and its aid, in condemnation of them, and in preventing the consequences which the act was designed to prevent, may be invoked by the receiver representing the creditors for whose benefit the statute was enacted" (309 U. S. at 198–199). Reliance was placed in the *Deitrick* case on the fact that the maker of the note was a participant in an illegal transaction. The court, however, did not base its decision on the ground that the execution of the note, as distinguished from the bank's purchase of its stock, was within the express condemnation of the statute. In concluding that the concealment of the stock purchased by means of an accommodation note was unlawful, the court relied on the purposes of the Act to prevent impairment of the capital resources of national banks and to insure prompt discovery of violations through periodic examinations and reports. The legal consequences of the implied statutory condemnation of the transaction were held to be questions of federal law. The Supreme Court resolved the questions in the light of the policy of the National Banking Act and accordingly held defendants liable.

In *D'Oench, Duhme & Co.*, v. *F. D. I. C., supra,* the Federal Deposit Insurance Corporation, which had insured a bank after audit by bank examiners, brought

suit to recover on notes given by defendant to the bank, on an agreement that the notes would not be called, for the purpose of permitting the bank to avoid having its records show any past due bonds. Concededly, defendant and the bank had not arranged to use the notes for the express purpose of deceiving F. D. I. C. on insurance of the bank. Nevertheless, the result of the transaction was to misrepresent the assets of the bank to its creditors and to the bank examiners upon whose audit F. D. I. C. relied. Such a misrepresentation if it had been made knowingly and with intent to influence in any way the actions of the F. D. I. C. would have been a felony under Section 12B (s) of the Federal Reserve Act, 12 U. S. C. 264 (s). The Supreme Court viewed the case as presenting a question of federal law and held that the provisions of the Federal Reserve Act "reveal a federal policy to protect respondent, and the public funds which it administers against misrepresentations as to the securities or other assets in the portfolios of the banks which respondent insures or to which it makes loans." *Id.* at 457. Defendant having violated that policy by causing a misrepresentation *without criminal intent* to do so, was held liable.

In the case at bar, appellees have aided in the conversion of property mortgaged to the United States. Their act, in so doing, was in violation of a federal

policy aimed at protecting the Administration and the public funds. Questions as to their liability are federal questions to be determined in the light of the policy announced by Section 658 and that policy requires that the generally accepted commercial rule (see pp. 17–19, *supra*) be applied to hold defendants liable in conversion. *Deitrick* v. *Greany, supra; D'Oench, Duhme & Co.* v. *F. D. I. C., supra.*[16]

CONCLUSION

For the reasons stated, it is respectfully submitted that the judgment below should be reversed and the cause remanded with instructions to enter judgment for the United States for the full market value of the livestock which appellees sold without the consent of the mortgagee Farmers Home Administration, less any

[16] It is true that in *Kramel*, the Eighth Circuit held that these cases were distinguishable on the question as to whether state or federal law governed, expressing the opinion that (234 F. 2d at 582) in both "there were either direct expressions in the particular Act involved or clear intimations that Congress intended uniformity of administration of the respective act under federal control instead of use of State law." While we think this distinction without merit (see pp. 13–16, *supra*), it is noted that the Eighth Circuit did not disagree that Section 658 reflected a federal policy which it would have had to take into consideration had it deemed the case to turn on federal law rather than Missouri law. And reading the *Kramel* opinion in its entirety, we think that it contains the plain implication that, had the Eighth Circuit determined that federal law was applicable, it would have held the commission merchant liable.

amount which the mortgagor may have refunded to appellant out of the proceeds of the sales.[17]

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[17] While it does not appear in the record, we have recently ascertained that, after the complaint was filed in the court below, Wheaton made restitution to the Government in the amount of $280.92. This sum reflects the net sales price of a cow, subject to the mortgage, which appellees sold on Wheaton's behalf on December 3, 1951 (R. 5). The restitution followed the entry by Wheaton of a plea of guilty to the charge that he had converted that cow in violation of 18 U. S. C. 658, *supra*. Insofar as the pertinent records disclose, no restitution has been made with respect to the other converted livestock involved in this case.

Since appellees are entitled to be credited with the above amount, their liability to the United States, while not extinguished, is in a sum less than that demanded in the complaint. In view of the fact that these matters are not of record, and of the additional fact that the cause would have to be remanded in any event for the ascertainment of the amount of interest due the Government, we believe that the credit against appellees' liability in conversion should be applied by the court below in the first instance. We are, of course, prepared to offer in that court the necessary documentary evidence as to the extent of Wheaton's restitution.

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